

UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK

-----X  
In Re: : 05-60006  
:   
REFCO, INC., : One Bowling Green  
: New York, New York  
Debtors. : September 11, 2007  
-----X  
TONE N. GRANT, et al, : 07-2005  
:   
Plaintiffs, :   
:   
v. :   
:   
AXIS REINSURANCE COMPANY, :   
:   
Defendant. :   
-----X

TRANSCRIPT OF HEARING  
BEFORE THE HONORABLE ROBERT D. DRAIN  
UNITED STATES BANKRUPTCY JUDGE

APPEARANCES:

For Plaintiffs: NORMAN L. EISEN, ESQ.  
Zuckerman, Spaeder, LLP  
1800 M Street, N.W.  
Washington, D.C. 20036  
  
For Messrs Grant:  
and Klejna HELEN B. KIM, ESQ.  
Baker & Hostetler, LLP  
333 South Grand Avenue  
Los Angeles, California 90071  
  
For Mr. Trosten: BARBARA MOSES, ESQ.  
Morvillo, Abramowitz, Grand, Jason,  
Anello & Bohrer, P.C.  
565 Fifth Avenue  
New York, New York 10017  
  
For Axis: JOAN M. GILBRIDE, ESQ.  
Kaufman, Borgeest & Ryan, LLP  
99 Park Avenue  
New York, New York 10016

(Appearances continued on next page)

UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK

APPEARANCES CONTINUED:

For Mr. Silverman:	RICHARD CASHMAN, ESQ. Heller, Ehrman, LLP Seven Times Square New York, New York 10036
For Messrs. Sexton and: Shearer	IVAN O. KLINE, ESQ. Friedman, Wittenstein & Hochman 600 Lexington Avenue New York, New York 10022
For RJM, LLC:	STEVEN WILOMOWSKY, ESQ. Bingham, McCutchen, LLP 399 Park Avenue New York, New York 10022
For Mr. Murphy:	JOHN J. JEROME, ESQ. Saul Ewing, LLP 1500 Market Street Philadelphia, Pennsylvania 19102
Court Transcriber:	SHARI RIEMER TypeWrite Word Processing Service 356 Eltingville Boulevard Staten Island, New York 10312

Proceedings recorded by electronic sound recording,  
transcript produced by transcription service

1 THE COURT: Grant v Axis Reinsurance in the Refco  
2 case.

3 MR. EISEN: Good morning, Your Honor.

4 Norman Eisen representing Mr. Grant and I will be  
5 arguing on the motion for advancement on behalf of Mr. Grant,  
6 Mr. Trosten and Mr. Bennett, although Mr. Trosten and Mr.  
7 Bennett's counsel are here as well and they may wish to join in  
8 at certain points.

9 THE COURT: Okay.

10 MR. EISEN: On behalf of everyone we want to thank  
11 the Court for taking the motion on an expedited basis. We  
12 believe that the fundamental issues that are raised by our  
13 advancement motion were raised and decided by the Court on the  
14 other insurance motion that we were before the Court on less  
15 than two weeks ago. As the Court knows, the criminal  
16 defendants -- we refer to them as the presumed innocent  
17 defendants in distinction to Axis' designation -- joined in the  
18 motion for advancement we argued, and the Court actually  
19 addressed in the course of its holdings -- actually addressed  
20 the prejudice to the criminal defendants with respect to the --  
21 on the balancing of harms.

22 I will just quickly go through the issues and I  
23 think reference to Axis' brief makes clear that fundamentally  
24 Axis is rearguing the issues that were before the Court the  
25 last time we were here on the question of what the standard is,

1 whether this is a prohibitory or mandatory injunction. The  
2 Court has already invoked the reasoning of WorldCom and ruled.  
3 The Court has applied the test of a likelihood of success on  
4 the merits or a sufficiently serious question and balance of  
5 harms. There is no new issue in the brief about, and we  
6 recognize the Court likely went to, the sufficiently serious  
7 question and balancing the harms prong of that test. The Court  
8 noted as much when it was ruling previously. There is no new  
9 issue in the papers about the likelihood of success on the  
10 merits or the sufficiently serious question going to the  
11 merits. It is a reargument of the clause relating -- the  
12 disputed clause and the Court has already ruled on that.

13 On the balance of the harms, we would submit that,  
14 again, as noted by the Court the harms are even more severe  
15 because the criminal defendants are facing trial; it's not  
16 merely a question of a risk of financial loss, it is a liberty  
17 interest and the most serious liberty interest, and any  
18 disruption in the preparation for trial as the Court noted is a  
19 very, very serious harm indeed.

20 One of the only -- I will not rehash absolutely  
21 every argument that the Court has heard ad infinitum in the  
22 many, many papers that have been filed. I'll attempt to focus  
23 on what's new in Axis' submission and the response. They do  
24 rely on a new case in addressing the balancing of the harms,  
25 that is the Gaon v. Twin Cities case. We obtained from Axis --

1 THE COURT: No one gave me a copy of that case.

2 MR. EISEN: Your Honor, we had the same problem --

3 THE COURT: And consequently I'm not going to  
4 consider it.

5 MR. EISEN: Okay. Then, Your Honor, really the  
6 only other significant --

7 THE COURT: Let me -- it's an unpublished  
8 decision.

9 MR. EISEN: Yes, it is, Your Honor.

10 THE COURT: You're all familiar with the Second  
11 Circuit rule on citing unpublished decisions. If I were to  
12 consider it as persuasive authority, simply like a law review  
13 article or the like, I would have expected the parties to have  
14 provided it to me since I prepare in advance for these things  
15 and this is a preliminary injunction hearing and that's not  
16 been done and so I'm not going to consider it.

17 MR. EISEN: Understood, Your Honor, and we  
18 certainly are not relying on it and you won't hear anymore  
19 about it from us.

20 The only other issue of significance that is new  
21 in the papers is the priority of payments issue and that popped  
22 up, really, yesterday with the filing of Axis' opposition and  
23 then of the motion to intervene. With respect to proposed  
24 intervenors' issues, we conferred with them before court this  
25 morning and we've also informed Axis of this, the movants today

1 are satisfied to have the identical form of order that the  
2 Court entered last time with the addition of the proposed  
3 language that Mr. Klejna's counsel has requested, which is to  
4 the effect that nothing in this order shall affect the priority  
5 of payments issue. We really do not view the priority of  
6 payments issue as procedurally appropriate for a decision  
7 before the Court. It has not been teed up. It is not ripe.  
8 We don't know if there is a disagreement yet. We haven't had a  
9 chance to evaluate it. Obviously, there's been no factual  
10 development, there's been no briefing. It really is a last  
11 ditch attempt to interpose an obstacle to the payment of the  
12 fees that the movants today so desperately need in order to  
13 avoid disruption of the criminal case.

14 So, the issues really being the same, we would  
15 submit to the Court that it is a straightforward application of  
16 the decision that the Court has already rendered and, indeed,  
17 was prepared to render but for the Court's request that we file  
18 an adversary proceeding of our own and a motion for preliminary  
19 injunction which we've done.

20 THE COURT: What is the -- and there was some  
21 confusion about this last time -- billed amount of the defense  
22 costs for the three defendants?

23 MR. EISEN: Your Honor, Axis has provided that  
24 information on Page 30 of their opposition and I'll go over  
25 that and then I will relate an issue -- conversation that we

1 all had amongst ourselves in the hallway just updating that and  
2 I know Axis' counsel will correct me if I err.

3 When we were before the Court the last time the  
4 total amount was in the neighborhood of \$2 million for Axis.  
5 As of Friday, the total amount at issue was in excess of \$2.9  
6 million. We certainly do not -- I think it's our position and  
7 the other insureds' position that none of us begrudge the  
8 payment of those sums to the others. Indeed, for the criminal  
9 defendants it is crucial because the pipeline is building up  
10 and we have so much work to do and the consequences are so  
11 great. We would ask the Court to order payment of that amount.  
12 Approximately \$300,000.00 of that \$2.9 million has already been  
13 paid down or is in the process of being paid down.

14 THE COURT: Well, let me make sure of that. The  
15 aggregate number you gave me, the \$2 million as of last Friday  
16 --

17 MR. EISEN: It's \$2.9 million, Your Honor, as of  
18 Friday.

19 THE COURT: I'm sorry. Then there was \$2 million  
20 as of the hearing that we had.

21 MR. EISEN: Yes, Your Honor.

22 THE COURT: That includes the defense costs of  
23 which defendants?

24 MR. EISEN: I believe that includes the defense  
25 costs of all of the parties who were before the Court on the

1 previous motions and --

2 THE COURT: Well, let me make sure. It does not  
3 include Mr. Lee; right?

4 MR. EISEN: I do not know if it includes or not.  
5 I can speak for the five insured individuals represented by  
6 Baker, Hostetler and the other firms and I can speak for the  
7 three criminal defendants. I cannot at all speak for Weil,  
8 Gotshal's clients, for Mr. Lee. I'm sure Ms. Gilbride knows  
9 the answer to that question. I do not.

10 THE COURT: All right.

11 MR. EISEN: And just to update the Court there  
12 have been approximately \$1 million in additional invoices that  
13 have come in over the weekend and yesterday.

14 MS. GILBRIDE: I believe that is correct. I  
15 actually anticipated -- to correct you since we're on this  
16 topic, I think the \$2.9 million as of Friday does include the  
17 Thomas H. Lee fees.

18 THE COURT: It does. Well, as far as the  
19 defendants represented by Ms. Kim and Mr. Goodman, the ones  
20 represented by Baker & Hostetler, I gather that that was about  
21 \$300,000.00/\$307,000.00; is that right?

22 MS. GILBRIDE: That's correct, Your Honor.

23 THE COURT: And I'm taking that away for the  
24 record in the district court?

25 [Pause in proceedings.]



1 MS. GILBRIDE: Oh, as of the earlier hearing, Your  
2 Honor.

3 THE COURT: Right.

4 MS. GILBRIDE: Not as of today.

5 THE COURT: Right. No, I understand.

6 MS. KIM: Your Honor, the \$307,000.00 was as of  
7 August 30th for the five officer defendants that moved as of  
8 that day.

9 THE COURT: All right. All five of them?

10 MS. KIM: All five, not just the Baker, Hostetler  
11 --

12 THE COURT: So that's not just Baker & Hostetler  
13 but all five.

14 MS. GILBRIDE: All five of the moving parties;  
15 right.

16 THE COURT: All right. Do we know how much is for  
17 the movants today in the aggregate? The three?

18 MR. EISEN: Your Honor, I --

19 THE COURT: Well, no, no, no, let me hear the  
20 answer.

21 MS. GILBRIDE: Your Honor, my understanding is as  
22 of yesterday for just these moving parties it's \$2.9 million.

23 THE COURT: Just them?

24 MS. GILBRIDE: Just them.

25 THE COURT: Just these three?

1 MS. GILBRIDE: Yes, Your Honor.

2 MS. MOSES: Your Honor, Barbara Moses, Your Honor,  
3 for Robert Trosten.

4 THE COURT: Well, let me make sure -- there's some  
5 conferring going on over here.

6 [Pause in proceedings.]

7 THE COURT: Just these three?

8 MS. GILBRIDE: Yes, Your Honor.

9 THE COURT: And how much as of the date that I  
10 ordered the -- would you have this number as of the date that I  
11 ordered the payment for the five represented --

12 MS. GILBRIDE: Yes. Yes, that would be \$1.6.

13 THE COURT: \$1.6.

14 MS. MOSES: These are the three numbers for us.

15 THE COURT: Okay. But that would be just for  
16 these three --

17 MS. GILBRIDE: Yes, Your Honor.

18 THE COURT: -- as of the date of the earlier order  
19 that I entered?

20 MS. GILBRIDE: Correct. As of August 31st; right.

21 THE COURT: Okay. Go ahead.

22 MS. MOSES: I apologize, Your Honor. I was  
23 conferring with Mr. Eisen and I missed your last exchange with  
24 Ms. Gilbride. This is Barbara Moses speaking on behalf of  
25 Robert Trosten. But we, the three movants before the Court

1 this morning, have added up our numbers among ourselves and  
2 they don't add up to \$2 million.

3 THE COURT: Well, okay. I asked Ms. Gilbride two  
4 questions; one was as of the most recent date and that was \$2.9  
5 and I understood, and then I asked as of August 31st which was  
6 the date of my earlier order, and that was \$1.6 million. Have  
7 you broken it out that way too?

8 MS. MOSES: Well, my understanding, Your Honor --  
9 and co-counsel for today's moving parties will correct me if I  
10 am wrong -- but my understanding is that as of August 30th the  
11 three plaintiffs who are before you today had submitted bills  
12 totaling -- I'm doing this in my head so bear with me while I  
13 round -- approximately \$940,000.00 or maybe \$950,000.00.

14 THE COURT: Okay.

15 MS. GILBRIDE: We received substantial bills just  
16 yesterday from --

17 THE COURT: No, we're just focusing right now --

18 MS. MOSES: Right. That was the August 30th  
19 figure.

20 MS. GILBRIDE: Okay. From Kramer, Levin.

21 THE COURT: -- as of August 31st.

22 MR. EISEN: Yes, that was included.

23 MS. GILBRIDE: Okay.

24 [Pause in proceedings.]

25 THE COURT: So you include bills that cover the

1 period through August 30th in that \$950,000.00 number?

2 MS. MOSES: Your Honor, I'm going to apologize and  
3 correct myself on the record. Mr. Eisen tells me that my  
4 figure was incorrect.

5 THE COURT: Okay. So is it as of August 31st it's  
6 really \$1.6 million?

7 MR. EISEN: It's \$1.6 million to \$1.7 million,  
8 Your Honor.

9 THE COURT: Okay.

10 MS. GILBRIDE: That's the same number we have.

11 THE COURT: Okay.

12 MR. EISEN: Then, just so I'm clear if I may ask  
13 Axis through the Court it then goes up to \$2.6 as of Friday  
14 when the papers were filed according to Axis' motion at Page  
15 30, Paragraph 65, as of Friday, September 7th, Axis had defense  
16 bills with a value of over \$2.9, of this amount \$307 was  
17 subject to the Court's August 31st order so \$2.9 minus \$300 is  
18 \$2.6 and then as of the weekend and yesterday it is up to \$2.9.

19 THE COURT: Okay.

20 MS. GILBRIDE: Yes,

21 THE COURT: And what is that for? September?

22 MR. EISEN: No, Your Honor.

23 THE COURT: Is that the difference is September?

24 MR. EISEN: No. With the Court's leave I will  
25 explain the pipeline issue.

1           The firms have time going back to June that is in  
2     these bills because of the way they're billed at the end of the  
3     month.

4           THE COURT:   Okay.

5           MR. EISEN:   So you have June time, you have July  
6     time and how you have August time coming in because August has  
7     closed and the bills for August issue at the beginning of  
8     September.  From the perspective of the criminal defendants --  
9     and I don't believe that the other moving insureds who sought  
10    advancement and whose motion we previously joined disagree --  
11    what we would like to request the Court to do is to enter an  
12    order that would be -- really, the words of which would be  
13    identical to the order that was entered last time other than  
14    the caption and the introductory paragraph, which would provide  
15    that the bills should be paid through the date of the order  
16    subject to the proviso that nothing in the order affects the  
17    priority of payments because, you know, none of us wants -- we  
18    recognize as the Court noted previously that it is a narrow  
19    ruling confined to the obligation to advance that does not get  
20    into other issues.  I would only add that in terms of the  
21    equities or the harms to have -- we are already going to be  
22    carrying September time while we wait for the issue to be  
23    resolved.  We are at the point of having to undertake, as is  
24    obvious from the bills, very substantial work to get ready for  
25    trial which is in March, and I really think it goes to the

1 spirit and the letter of the cases to -- obviously, I'm not  
2 asking the Court to issue an injunction that carries forward.  
3 I recognize that there's going to be a motion for summary  
4 judgment heard in October but in order to avoid disruption it's  
5 important to have some lessening of the liabilities hanging  
6 over the clients in the pipeline, and the other movants agree  
7 with that provided the language is inserted about the priority  
8 of payments.

9 THE COURT: Well, let me make sure I understand  
10 that. I mean I can certainly see them making the argument that  
11 they moved first for an injunction and I approved -- ordered  
12 the payment of their defense costs through the date of the  
13 earlier order so they're in essence now a week or so behind and  
14 that may be a meaningful week because of month-end billing, and  
15 so you're saying they don't oppose your sort of jumping ahead  
16 by that extra billing?

17 MR. EISEN: Your Honor, I think they would ask  
18 that that be reciprocal that it also apply to them so the --  
19 and I think that that is --

20 THE COURT: Well, let me hear from them. They're  
21 standing up behind you so --

22 MR. KLINE: Your Honor, Ivan Kline from Friedman,  
23 Wittenstein for two of the other movants, Mr. Sexton and  
24 Mr. Shearer. I know I'm speaking also for Mr. Silverman. I  
25 believe -- because we joined in the same comment with Baker &

1 Hostetler -- our position is that it should be limited to the  
2 same date, August 31st or August 30th, whichever it was --

3 THE COURT: The date of that order.

4 MR. KLINE: And they should not be jumping ahead.  
5 And let's be realistic, a bill sent for August time on  
6 September 8th is really not due now in any event and lawyers  
7 all the time carry their bills for thirty days. We didn't get  
8 payment from U.S. Specialty or Lexington in, you know, a week  
9 after the bills were submitted and in all fairness,  
10 understanding the situation they're in is really -- we could  
11 all wait until October 12th for the bills that are being sent  
12 out in September. That is our position and that this order  
13 should not go beyond the same August 31st cutoff under any  
14 circumstances.

15 THE COURT: All right. Ms. Kim, is that the view  
16 for your clients as well?

17 MS. KIM: Yes, Your Honor. However, if you are  
18 inclined to grant that as of this date --

19 THE COURT: No, I understand.

20 MS. KIM: Then, of course, we'd want to be brought  
21 to the same and not falling behind, Your Honor. That's all.

22 THE COURT: Right. Okay. All right.

23 MR. EISEN: Your Honor, our view is -- and I  
24 apologize, I had understood from my conversation from Ms. Kim  
25 that she was comfortable, in fact I circulated a form of order

1 that provided today and I had understood that others were  
2 comfortable with that form of order and --

3 THE COURT: Well, as long as they were going to  
4 get pushed up, but I phrased my question with the assumption  
5 that they weren't --

6 MR. EISEN: I apologize if I did not understand  
7 the admittedly rushed conversation in the hallway.

8 Your Honor, the criminal defendants, though, would  
9 submit to the Court that there are different exigencies that  
10 apply to our need and if I may the clients will be facing the  
11 prospect of uncertainty as you've heard from Axis very  
12 substantial August bills on top of very substantial September  
13 bills. It's not just the question of Axis having agreed to pay  
14 and waiting a reasonable amount of time for the invoice to be  
15 honored, it is the uncertainty and the precise chilling effect  
16 on the ability to defend the case that the WorldCom court was  
17 concerned with when it balanced the harms. I do think in  
18 fairness that if the Court were to order this relief that it  
19 ought to apply to the intervening parties as well, but the  
20 criminal defendants are really in a unique situation because of  
21 the pendency of the criminal case and it will have a disruptive  
22 effect on the ability to defend that case. They will be  
23 incurring enormous costs, and so I would ask the Court in a  
24 balanced way that also recognized the needs of the intervenors  
25 and for that matter of Axis with respect to priority of



1 payments to enter the order that allows us to limit some of the  
2 backlog. We're not insisting that those bills be paid  
3 tomorrow. Axis can take a reasonable amount of time to  
4 evaluate them. I understand that there were some deductions  
5 that they applied to the bills that the others who were before  
6 the Court a little less than two weeks ago submitted and we  
7 don't have any objection to the normal course. What is  
8 difficult for us is to arrive at mid-October carrying millions  
9 of dollars in fees for August and for September not knowing  
10 whether our clients are going to be able to defend the criminal  
11 case. We think that the case law provides guidance to the  
12 Court that in those circumstances it is appropriate to award  
13 those fees and, frankly, the context is not irrelevant. We  
14 believe that Axis -- well, I certainly won't rehash the  
15 argument -- we think that Axis should have advanced these fees.  
16 The first two layers of insurance did advance the fees, we've  
17 been in this position of jeopardy for some time and, you know,  
18 Axis could have avoided today by, once the Court made its view  
19 of the law and the facts clear, agreeing to advance fees we  
20 would not be here. So to some extent Axis has proceeded at its  
21 peril. We think that that raises issues about the good faith  
22 of the insurer but that at any rate it is fair and right and  
23 equitable for the criminal defendants to have the pipeline  
24 lessened somewhat.

25 THE COURT: Do you or the other two movants have

1 any factual showing that you want to make in respect of the  
2 issue of whether, in no particular order, if I ruled -- or  
3 whatever court had jurisdiction over this matter ruled --  
4 against them ultimately that they could reimburse the money  
5 advanced? That would be one issue. The other issue is their  
6 ability to pay currently, themselves, and, I guess, the third  
7 issue is as to the defense counsel's willingness to proceed  
8 with this issue hanging over them. Or do you intend to rely on  
9 the logic that Judge Cote set forth in WorldCom?

10 MR. EISEN: Your Honor, I'll take those --

11 THE COURT: In no particular order.

12 MR. EISEN: -- in no particular order. I think  
13 there are two guiding precedents; one is the WorldCom case on  
14 your first question and the other is this Court's decision two  
15 weeks ago and this is the exact argument that the insurers made  
16 in WorldCom. I'll just read from the opinion at 469 to 470,  
17 "Continental and Twin City argue that Roberts has failed to  
18 show irreparable injury because he has not shown that he is  
19 unable to retain counsel from his own funds." And then later on  
20 the WorldCom Court also addresses the argument about  
21 reimbursement and the Court says, "the issues here surmount  
22 whether an individual director has or does not have sufficient  
23 funds to pay counsel when confronted with litigation stemming  
24 from services of a corporate director. In some cases it will  
25 be minor [here it is massive], in some cases a director will

1 have great personal wealth, in other cases she will not. The  
2 issue here is whether every director is protected by a policy  
3 to have the ongoing payment of defense costs." So we think  
4 that WorldCom -- that that's the wrong question under WorldCom.  
5 This is a -- as the Court noted at 87 to 88 of the transcript,  
6 this is a massive litigation. As demonstrated, the Court has  
7 the evidence about the size of the bills, it has the evidence  
8 about the pending civil cases that it relied on when we were  
9 last before the Court. It certainly is aware of the pending  
10 criminal cases, and, respectfully, Your Honor, we think that  
11 the case law does not require that question to be answered and  
12 for the same reason that the Court advanced previously it's  
13 appropriate to do so as of today or if the Court -- really, as  
14 of today as to all the insureds. We're not asking for special  
15 treatment. It really is as to all the insureds and we wouldn't  
16 be here but for Axis' refusal to do that. Indeed, for their  
17 refusal to do something less.

18 THE COURT: Okay. What about the other two  
19 defendants on that particular question?

20 MS. MOSES: Thank you, Your Honor. Barbara Moses  
21 for Mr. Trosten.

22 I concur in Mr. Eisen's remarks. I would also  
23 point out that by asking the question together, by coupling the  
24 two questions of ability to pay defense costs currently and  
25 ability to repay in the event the case ultimately is determined

1 differently, I think Your Honor may have fallen into, perhaps  
2 just on a testing the waters basis, what's really a Catch-22  
3 that the carrier would like to set up. On the one hand, they  
4 have urged Your Honor -- and Your Honor rejected this on August  
5 30th, correctly we believe -- on the one hand they urged Your  
6 Honor to require the insureds to prove that they are broke in  
7 order to get the advancement to which they are contractually  
8 entitled but then in the next breath they have urged Your Honor  
9 to rule that if the insureds are broke relief should be denied  
10 because they will be at risk of non-repayment should the case  
11 turn out adversely later in the day. It seems to me, Your  
12 Honor, that common sense and ordinary principles of equity tell  
13 you that they can't have it both ways. With respect to the  
14 ability to repay, let me make the following, I think, also  
15 common sense comment which is that the ability of an insured  
16 who is facing criminal charges and is subject to a pre-trial  
17 asset freeze order to repay at the conclusion of the criminal  
18 trial depends in large part on how that trial comes out. Now,  
19 Axis, I think, would like for my client and the other criminal  
20 defendants to lose their criminal trial because they will then  
21 use that in the coverage dispute, but with respect to the  
22 ability to repay I say to you that we need the defense costs  
23 now in order to insure that the criminal trial comes out in  
24 favor of our clients, which in turn has a bearing on the  
25 ability to repay at the end of the day.

1 THE COURT: Okay.

2 MR. GOLENBOCK: Your Honor, Jeffrey Golenbock for  
3 Mr. Bennett.

4 I would like to rely on the arguments that have  
5 been made by my colleagues. I don't think I need to add  
6 anything further. I'll, of course, answer any questions Your  
7 Honor may have.

8 THE COURT: Okay. Thank you.

9 Ms. Gilbride.

10 MS. GILBRIDE: Your Honor, the first thing I'd  
11 just like to note for the record is that we have gone ahead as  
12 suggested by Your Honor during the August 30th hearing and made  
13 a motion to withdraw the reference. I think it is important  
14 for the Court to be aware of that. Perhaps you are already  
15 aware of that.

16 THE COURT: I was. Yes.

17 MS. GILBRIDE: Okay. That motion is before the  
18 district court. We're not quite sure where we are procedurally  
19 with that so I can't report back where we are and when there's  
20 going to be a hearing. We have certainly asked that there be a  
21 hearing expeditiously. I believe that there will be, but we  
22 face substantial opposition from the insureds with respect to  
23 going that route as suggested by Your Honor on August 30th.

24 In any event, I don't believe we're here today in  
25 the same posture that we were here on August 30th. First of

1 all, the three moving parties here today initially moved to  
2 dismiss Axis' complaint. They joined in that motion. That  
3 motion was granted by Your Honor. They have now turned around  
4 and instituted an adversary proceeding seeking the same relief  
5 sought by other moving parties and, Your Honor, I would suggest  
6 that that is just fundamentally unfair and an abuse of the  
7 legal system by these moving parties.

8           Additionally, Your Honor, these three defendants  
9 are not in the same posture, on any test, particularly, one of  
10 the three moving parties, as the moving parties on August 30th  
11 who requested the preliminary injunction. One of these parties  
12 is the individual who signed the warranty letter that Axis  
13 relied upon. He's the individual who signed the application,  
14 he's the individual whom the company disclosed in an SEC filing  
15 three days after -- excuse me, shortly after the company went  
16 public that he had hidden \$430 million worth of receivables.  
17 Well, that was information that Axis relied upon as well. So,  
18 Your Honor, I submit we are not in the same position that we  
19 were in on August 30th.

20           With respect to the preliminary injunction, Your  
21 Honor, I apologize first of all that we did not attach the Gaon  
22 transcript. It's not a published decision. It's a transcript.  
23 It was before Your Honor on August 30th. It was submitted by  
24 Arch, who sought to intervene on that day. In any event, we'd  
25 be happy to hand up a copy to Your Honor but you've already

1 made it clear that you're not going to rule upon it. This  
2 preliminary injunction was brought on very quickly as Your  
3 Honor is aware and we apologize, again, for not submitting that  
4 but I would strongly urge that the Court consider the  
5 propositions that were articulated in that ruling, which  
6 essentially our position is that what Judge Wood did was simply  
7 apply Second Circuit case law which is clear that if you're  
8 going to apply the lower standard for injunctions there has to  
9 be a balancing of harms. There's been no factual record made  
10 before this Court; not one affidavit, not one individual has  
11 come here to testify before Your Honor with respect to the  
12 irreparable harm that they have allegedly suffered. There is  
13 no factual record before Your Honor, and I submit under Second  
14 Circuit law that is simply fatal to an application for a  
15 preliminary injunction.

16           Going to the balancing of harms, Your Honor, you  
17 know, on the one hand you have individuals who have made no  
18 factual showing whatsoever but who have come before Your Honor  
19 and said that their defense is going to be devastated because  
20 their defense counsel is not paid. Well, I submit that that  
21 should have been submitted to Your Honor in factual form.  
22 There should have been evidence submitted to your Court of  
23 that, not counsels' statements. But in any event, so there's  
24 no factual showing.

25           On the other side of the coin you have an

1 insurance company who has a policy provision that says if we  
2 are ultimately successful we are entitled to repayment. The  
3 movants are here on a preliminary injunction. Rule 65 provides  
4 the answer to all of these questions. If the Court is inclined  
5 to grant the preliminary injunction, Your Honor, we would  
6 suggest that the Court require the moving parties to post a  
7 bond or some form of security so that in the event some court  
8 agrees with Axis' position and finds that we have been  
9 wrongfully enjoined that there is then some security for Axis  
10 with respect to repayment. Otherwise, Your Honor is advancing  
11 something -- advancing relief to these parties on a very  
12 preliminary basis without a full-blown hearing, with Axis'  
13 complaint having been dismissed. So with Axis not having the  
14 ability to present its arguments in any shape or form and not  
15 even requiring a factual showing by the parties and, you know,  
16 Your Honor, we would submit under those circumstances at the  
17 very least that the Court order these moving parties to post  
18 some form of security in the event that Axis is successful.

19           You know, under the circumstances it's clear that  
20 Axis has zero prospect of being repaid if at the end of the day  
21 Axis is actually successful in whatever form we are able to  
22 actually litigate our dispute.

23           With respect -- I don't know if you want to get  
24 into the priority of payments issue, Your Honor -- the issue we  
25 have there is that separate and apart from defense costs there



1 has been an executed MOU submitted to Axis, and as of today if  
2 some court ultimately finds that there is actually coverage  
3 under the policy and we are required to fund that settlement --  
4 if the court says we should have considered that settlement as  
5 of the date the settlement was executed, Your Honor will be  
6 ordering us to advance defense costs in excess of our policy  
7 limits. Now, we are not at liberty to share that MOU with you  
8 but --

9 THE COURT: But you aren't paying under the MOU;  
10 right? Your clients aren't making a payment. It's disputing  
11 the coverage, I think.

12 MS. GILBRIDE: Well, we've been asked to fund the  
13 settlement.

14 THE COURT: I know but you're not paying it.

15 MS. GILBRIDE: I don't know that any determination  
16 has been made. Whether we are going to fund it or not has not  
17 come to fruition.

18 THE COURT: But I thought that Axis disclaimed  
19 coverage?

20 MS. GILBRIDE: Well, we did, Your Honor, but you  
21 know, there's a moving target in terms of what the Court is  
22 ordering us to do here.

23 THE COURT: Well, but all I'm saying is the  
24 individual -- I'm assuming it's an individual -- who submitted  
25 the proposed settlement hasn't sought relief to compel payment;

1 right?

2 MS. GILBRIDE: Not yet.

3 THE COURT: Okay. So how does requiring payment  
4 of the defense costs, to somebody who hasn't sought that relief  
5 -- and I'm assuming that anyone whose the beneficiary of the  
6 policy knows that if this litigation is going on and would make  
7 the same application that if they really wanted to enforce it,  
8 but hasn't -- how does my ordering the -- if I were to do it --  
9 the advancement of the defense costs put the insurer at a  
10 disadvantage?

11 MS. GILBRIDE: Your Honor, historically, the  
12 defense costs have been reimbursed by the two underlying  
13 carriers on a first in/first out basis. So if one was to  
14 consider the settlement as of the date it was executed in that  
15 line of payments and we do ultimately -- we are required to  
16 fund the settlement -- by advancing these defense costs now, we  
17 could theoretically or we would be asked -- we are being put in  
18 a position where we potentially are paying fees --

19 THE COURT: Well, when was the MOU submitted?

20 MS. GILBRIDE: When was it executed? August 30th.

21 THE COURT: Well, what --

22 MS. GILBRIDE: Well, it was signed on August 30th.

23 THE COURT: But when was it submitted to the  
24 insurer?

25 MS. GILBRIDE: July 30th.

1 MR. EISEN: No.

2 MS. KIM: Yes, July 30th.

3 MR. EISEN: The MOU submitted --

4 THE COURT: But it was signed after it was  
5 submitted?

6 MS. KIM: Your Honor, may I address that issue?

7 THE COURT: Okay.

8 MS. KIM: Helen Kim on behalf of Mr. Klejna, Your  
9 Honor. The MOU which was a settlement demand from the lead  
10 plaintiffs in the underlying securities litigation in In Re:  
11 Refco securities litigation was submitted to Axis on July 30th  
12 on the date it was received by Mr. Klejna.

13 THE COURT: Okay.

14 MS. KIM: With a request to Axis to assist in the  
15 settlement and to --

16 THE COURT: To assist, but as far as a settlement  
17 itself, when was that submitted as a settlement?

18 MS. KIM: Well, we requested Axis to join the  
19 negotiations because they have an obligation under the policy  
20 to consent to settlement.

21 THE COURT: All right. But as far as an  
22 obligation to pay money in respect of a settlement --

23 MS. KIM: Well, Your Honor, it is our position  
24 that Axis has an obligation, once it's presented with a signed  
25 settlement agreement, to either consent or not consent and so

1 it has to set aside money for a settlement if it consents.

2 THE COURT: I'm sorry, it wasn't signed when it  
3 was submitted to them in July; right?

4 MS. KIM: Not on July 30th but after --

5 THE COURT: It was signed at the end of August;  
6 right?

7 MS. KIM: It was signed on August 30th after Axis  
8 gave us -- told us to proceed as a prudent uninsured and to  
9 proceed accordingly.

10 THE COURT: Okay. So wouldn't that be the  
11 relevant date then?

12 MS. KIM: August 30th; correct, Your Honor.

13 THE COURT: Okay.

14 MS. KIM: So what we're saying is -- and this goes  
15 to the issue of priority of payments -- as long as any order on  
16 the preliminary injunction does not interfere with the priority  
17 of payments under the terms of the Axis policy we don't believe  
18 that there's a problem.

19 THE COURT: Okay. How would it interfere? Say I  
20 were to require payment of these three individuals' defense  
21 costs as of the date of my order which, I forget, was that  
22 either August 30th or 31st?

23 MS. GILBRIDE: The 31st.

24 THE COURT: How would it interfere with this  
25 separate potential obligation?

1 MS. KIM: It would not, Your Honor.

2 THE COURT: Well, no, I was asking Ms. Gilbride.

3 MS. KIM: Oh, I'm sorry.

4 MS. GILBRIDE: If you were to order today as of  
5 August 31st?

6 THE COURT: Yes.

7 MS. GILBRIDE: We're just trying to look at the  
8 numbers and figure this out. We were anticipating that Your  
9 Honor might be inclined to award advancement of defense costs  
10 as of today.

11 THE COURT: No, well, that wasn't my question.

12 MS. GILBRIDE: Okay. I know. So I don't have the  
13 answer readily available. I apologize.

14 MS. KIM: If it's \$2.1 million as of August 31st  
15 which were the numbers that we discussed earlier, there would  
16 be nothing, Your Honor. No interference whatsoever.

17 THE COURT: All right.

18 MS. GILBRIDE: Your Honor, I think that if it was  
19 as of August 31st I agree that we would still be within the  
20 policy limits.

21 THE COURT: All right. I'm not saying that that's  
22 where I'm going on this. I'm not saying that's -- no one  
23 should read this as a determination of any allocation or  
24 priority issues.

25 MS. KIM: We understand, Your Honor.

1 THE COURT: It's just that we're trying to figure  
2 out the facts.

3 MS. KIM: That's right, Your Honor, and we agree  
4 with Your Honor.

5 MR. EISEN: Your Honor, were the Court to decide  
6 to enter the identical order as last time effective as of  
7 today, the date of the order, it could also address this issue  
8 by simply including the sentence that Ms. Kim requested. We  
9 and Ms. Kim's clients agree on that, that this order does not  
10 affect the priority of payments in any way.

11 THE COURT: Well, I know that an order can say  
12 that, but as a practical matter it might wouldn't it?

13 MR. EISEN: No, Your Honor, we think it would not  
14 because the insurer is perfectly capable, as they've  
15 demonstrated, of taking positions on the legal issues. The  
16 priority of payment issue is, we think, a make-weight issue.  
17 The settlement has not been presented, much less approved.  
18 They could certainly pay up to the limits without any risk.

19 THE COURT: Well, no, let me -- as I understand  
20 Axis' point, it's this, that although they have disclaimed  
21 coverage, ultimately they might have to pay on the settlement,  
22 and since the settlement came in as of a date that preceded  
23 some of these bills, you know, the ones in September, they  
24 would be paying these bills -- the post-September bills --  
25 potentially out of sequence, first come/first serve. Now,

1 maybe that's not right, maybe that priority doesn't depend on  
2 first come/first serve necessarily, but that's their point.

3 MR. EISEN: Your Honor --

4 THE COURT: And they wouldn't have any ability  
5 necessarily to get it back or reallocate it, necessarily.

6 MR. EISEN: Your Honor, the issue is clouded  
7 because the amount of the settlement is unknown. However, I  
8 can represent to the Court based on conversations with various  
9 persons attempting to determine, you know, would you pay the  
10 bills as of the beginning of September, mid-September, so on  
11 and so forth, that the -- we believe it would be possible to,  
12 without implicating the priority of payments issue at all, to  
13 pay the bills through Friday. But, again, there is a safe  
14 harbor for this, which is simply to provide in the order to  
15 have us agree that pending the resolution in October the  
16 insurer only needs to pay up to the amount of the settlement.  
17 If, for example, the settlement is \$6.5 million --

18 THE COURT: No, I understand your point. All  
19 right. So that would be a cap --

20 MR. EISEN: That is a way to accommodate the harms  
21 that the criminal defendants are facing and at the same time  
22 give Axis a safe harbor.

23 THE COURT: Okay.

24 MS. MOSES: May I add a word, Your Honor, on the  
25 priority of payment issue? A word which is, I think,

1 particularly appropriate given Ms. Gilbride's comments  
2 concerning consistency in litigation position.

3 We were required to initiate a new adversary  
4 proceeding and to submit a pleading -- an adversary complaint --  
5 -- demanding payment of our defense costs in an ongoing schedule  
6 in order to properly put this issue before Your Honor and be in  
7 a position to ask Your Honor for a preliminary injunction for  
8 that relief. The settlement issue has never been teed up in  
9 any pleading. So, clearly, whether the Court has if you will  
10 jurisdiction to rule on it at this point --

11 THE COURT: Well, I don't think they're asking me  
12 to rule on it, I think they're saying that as far as the  
13 balance of the harms goes, I should take it into account.

14 MS. MOSES: Well, second, Your Honor, Ms. Gilbride  
15 has also asked Your Honor where's the evidence and has in  
16 effect asked Your Honor to ask us for evidence of financial  
17 condition, but, again, there has been no evidence presented to  
18 Your Honor of the settlement or its amount or any of its  
19 particulars, and, third, Your Honor, as we all know we have not  
20 had an opportunity to brief this point but as we all know from  
21 having practiced in federal court and under Rule 23 any  
22 settlement in In Re: Refco would have to be approved both  
23 preliminarily and finally after a notice and comment period by  
24 Judge Lynch before it would be binding on anyone.

25 THE COURT: Okay.



1 MR. EISEN: Your Honor, in addition to the very  
2 last point that Ms. Gilbride made, I do think that we and  
3 Ms. Kim's client and the other insureds agree that that  
4 language that she suggested to the order that this does not  
5 affect the priority of payments would allow the insurer to pay  
6 up to what's available and then provide a safe harbor for the  
7 rest.

8 May I very quickly be heard on Ms. Gilbride's  
9 other points?

10 THE COURT: Well, I hadn't finished asking her  
11 questions.

12 MR. EISEN: Okay. I'll sit down.

13 THE COURT: You can be, briefly, but after I -- I  
14 want to go back over something that we spent a lot of time on  
15 the last hearing, the interpretation of the provision of the  
16 U.S. Specialty policy that says the insurer will pay covered  
17 defense costs on an as incurred basis, and as I understand it  
18 Axis' argument is that these defense costs aren't "covered"  
19 under the policy?

20 MS. GILBRIDE: Yes, Your Honor.

21 THE COURT: But is that based simply on the  
22 exclusions?

23 MS. GILBRIDE: Yes. It's based upon the warranty  
24 and --

25 THE COURT: Well, the warranty is not part of the

1 policy is it?

2 MS. GILBRIDE: Well, it becomes part of the policy  
3 and it provides for its own remedy, Your Honor. It becomes an  
4 exclusion by its own terms. At the bottom of the warranty it  
5 provides that it becomes part of the policy and becomes an  
6 exclusion and it does not require any filing or adjudication of  
7 facts, it simply requires that Axis in good faith make a  
8 determination whether it applies to the facts before it and  
9 determine whether or not there's coverage.

10 THE COURT: Well, now you're moving away from the  
11 warranty to the overall argument?

12 MS. GILBRIDE: No, I was just saying what the  
13 remedy is that the warranty provides.

14 THE COURT: Okay. All right.

15 Then I guess my other question on this same  
16 contract issue is, you point to the following paragraph,  
17 Paragraph 3, which is dealing with the allocation of losses  
18 "covered" and losses "not covered" and say that that's further  
19 indication that the insurance carrier was given the authority  
20 under this contract to act unilaterally if it wasn't able to  
21 agree; and my question is, I guess, why go through that  
22 distinction at all in 3 if "coverage" pertains already? Why  
23 isn't that just a separate provision dealing with allocation?  
24 I mean if -- as I take it your first argument is you can act  
25 unilaterally as to whether something is "covered" or not. Why

1 would the parties then have a whole separate provision that  
2 would say the same thing?

3 MS. GILBRIDE: Your Honor, we pointed to condition  
4 (d)(3) simply as evidence that the entire policy should be  
5 construed in context. So our position is not that you should  
6 go to (d)(3) with respect to this dispute, we rely solely with  
7 respect to this dispute on (d)(1), but we rely upon (d)(3) as  
8 evidence to be in support of our position under (d)(2); (d)(3)  
9 is a provision that you actually utilize when there's covered  
10 and uncovered claims. So Your Honor is absolutely right that  
11 you would not utilize (d)(3) in this dispute. We were simply  
12 pointing it out to show that it is consistent with Axis'  
13 interpretation of (d)(2). Our position is that (d)(2) says in  
14 the first instance if defense costs are not covered, if the  
15 policy is not triggered, then Axis, acting in good faith, of  
16 course, would not have to advance defense costs.

17 THE COURT: Okay. Thanks.

18 MR. EISEN: Your Honor, I'll take them in order  
19 and I will attempt to be brief.

20 Ms. Gilbride's first point was that, after joining  
21 in the motion to dismiss, for us now to seek advancement is an  
22 abuse. As the Court well remembers, we did not just join in  
23 the motion to dismiss; in the alternative we also joined in the  
24 motion to advance, and in response the Court asked us to take  
25 procedural steps. We've done that. We've been crystal clear

1 throughout that we believe there's a legal obligation to  
2 advance, so I think there's no inconsistency there.

3 In terms of the factual record issue, I really  
4 would point the -- she first makes the point about irreparable  
5 harm and then about the balance of the harms. Our factual  
6 showing is exactly the same factual showing that the other  
7 moving insureds made. It's exactly the same factual showing on  
8 both of those points as was approved in WorldCom, so I think  
9 that this is an argument that was made and that was rejected  
10 and that does not --

11 THE COURT: Well, I guess the only distinction  
12 there is -- there seemed to be agreement between the parties  
13 last week that the five D's and O's that were covered by the  
14 injunction last week were fairly well-healed, and I mean that  
15 was a point that Axis made and no one really disputed it -- and  
16 that doesn't go to the point of irreparable harm but it does go  
17 to their other point about ability to reimburse and I  
18 understand your colleague's point about the Catch-22 or a  
19 Hobson's Choice, but I think that may be a distinction between  
20 last week's record and today's.

21 MR. EISEN: Your Honor, I do think it is clear in  
22 the WorldCom case that given the volume of the defense costs  
23 here -- for example, as the Court knows in the KPMG criminal  
24 litigation there was recently fact-finding by the district  
25 court about what it costs to defend these cases. Given the

1 volume, the precise -- you know, it is a harm on anyone and  
2 that that factual showing is not required, we think, under the  
3 case law.

4 I would also -- it goes to, I guess,  
5 Ms. Gilbride's repeated statements both here today and in the  
6 brief that there's zero prospect of repayment. That really  
7 turns the presumption of innocence on its head. We believe the  
8 clients will be acquitted. We're looking to the Court for the  
9 interim time so that we can keep working in September and at  
10 the beginning of October towards that goal and to presume that  
11 -- and Ms. Gilbride's conclusion really turns the legal  
12 presumption on its head -- we think that she's made the wrong  
13 analysis and she has not shown that there is zero prospect of  
14 repayment, and, of course, I think zero prospect is an  
15 overstatement.

16 On the priority of payments issue, we've already  
17 made the point that there is a solution, which is to include  
18 the language. And then the interpretation issues, we think,  
19 have already been decided by the Court and those are queued up  
20 for summary judgment, so I won't speak to those now unless the  
21 Court wishes me to.

22 THE COURT: Okay. Anyone else?

23 MR. CASHMAN: Your Honor, may I be heard for one  
24 moment?

25 THE COURT: Yes. Sure. I'm sorry, which one of

1 these movants do you represent?

2 MR. CASHMAN: I represent defendant Philip  
3 Silverman. He was among those who received the benefit of Your  
4 Honor's preliminary injunction last week.

5 THE COURT: Okay.

6 MR. CASHMAN: I just wanted to underscore, Your  
7 Honor, that I do not believe the issue of priority of payments  
8 is appropriately before Your Honor this morning. I think I  
9 would be remiss being here today, having listened to all these  
10 arguments, if I did not simply point out to Your Honor that  
11 there are various conflicting interests among the insureds that  
12 would have to be assessed in connection with any priority of  
13 payment argument that were made, and so I think the only issue  
14 that ought to be addressed here today is simply whether or not  
15 defense costs should continue to be advanced at the request of  
16 the moving defendants here and through what date, I think.  
17 Those are the only issues that need to be addressed and ought  
18 to be addressed, because all the other issues are complicated  
19 and raise varying issues that are not before you today and the  
20 policy itself does not offer a simple solution to those issues.

21 THE COURT: Okay. Well, let me hear somebody who  
22 hasn't spoken yet.

23 MR. WILOMOWSKY: Good morning, Your Honor. Steven  
24 Wilomowsky of Bingham, McCutchen, LLP on behalf of RJM, LLC,  
25 the plan administrator.

1           Your Honor, I just want to make a point on the  
2 record with regard to this motion, because the tie-in that  
3 brings these parties to this Court is the lift-stay aspect, is  
4 obviously the Refco aspect, but it does not follow necessarily  
5 that if the Court's analysis that led to the lifting of the  
6 automatic stay to the extent applicable for the other  
7 defendants necessarily applies to the movants that are here  
8 today. And the reason is, Your Honor, the movants today,  
9 particularly Mr. Bennett and Mr. Trosten, have not filed proofs  
10 of claim against the estates. Mr. Grant, also, though he did  
11 file a proof of claim, his claim has been estimated at zero  
12 dollars for all purposes including distribution.

13           To the extent that in considering today's motion  
14 Your Honor, taking into account impact on the estate, I think  
15 that there is a difference between just, for example,  
16 Mr. Klejna, who does have a claim filed against the estate and  
17 then, presumably, even though that hasn't been litigated or  
18 allowed or disallowed yet, but at least it's a claim that's  
19 there that potentially that any recoveries that they are able  
20 to get out of Axis or any other insurer is going to serve to  
21 reduce the claim against the Debtors' estates, whereas, with  
22 respect to the recoveries, for example, that may be achieved by  
23 Mr. Bennett, the only thing that's doing is really reducing  
24 availability of insurance proceeds for other people who do have  
25 claims and whose claims would be reduced if they were able to

1 receive insurance proceeds.

2           So we haven't taken a position in this litigation,  
3 it's been until now, certainly, it hasn't been -- early on in  
4 the cases there had been some involvement, we had been involved  
5 with Lexington, and it's been a close call among the plan  
6 administrators whether to -- this whole process is an expensive  
7 one and it's been a very time-consuming litigation for the  
8 parties here and so we've been reluctant to get involved,  
9 since, ultimately, there are no dollars -- there are no  
10 actually dollars that can come out of this policy that can come  
11 back into the estates, but we did want to say that to the  
12 extent that Your Honor is reviewing today's motion both in  
13 terms of its own jurisdiction and in terms of the lift-stay  
14 standards and elements, we would note that the estate is not  
15 going to be benefitted to the extent that, for example,  
16 Mr. Bennett were to recover from these proceeds.

17           THE COURT: Whether you take Judge Baer's version  
18 of it or Judge Gerber's version of it, doesn't Adelphia control  
19 here? I mean there's been -- at this point they're simply  
20 indicted, they're not convicted, and under the Adelphia case  
21 law, which I think is the most thorough discussion of this  
22 issue, wouldn't they be entitled to the money? Leaving aside  
23 issues of allocation which, again, I don't think I'm going to  
24 get into, but assuming that there are no allegation issues,  
25 don't they come first?



1 MR. WILOMOWSKY: Well, two responses to that.  
2 First, to the extent -- if one supposes that the automatic stay  
3 is applicable here and I understand that that could be an open  
4 question --

5 THE COURT: Well, I don't think there's -- people  
6 should stop talking about the automatic stay.

7 MR. WILOMOWSKY: Okay.

8 THE COURT: It's a plan injunction.

9 MR. WILOMOWSKY: Okay.

10 THE COURT: The confirmation order is really clear  
11 on this in Paragraph 34.

12 MR. WILOMOWSKY: Okay. That's correct, Your  
13 Honor.

14 THE COURT: So when people are saying "automatic  
15 stay" I'm translating it in my head --

16 MR. WILOMOWSKY: They mean --

17 THE COURT: -- the plan injunction.

18 MR. WILOMOWSKY: Okay. You got it, Your Honor.

19 THE COURT: So that's what we're talking about.

20 MR. WILOMOWSKY: All right. In response to your  
21 question I think that the differences here is that at least  
22 what Adelphia speaks to is the access that the parties can have  
23 to the policy notwithstanding the fact that they may be under  
24 criminal indictment or whatever their situation might be. I  
25 think it's a separate question as to -- and I may be

1 misremembering Adelphia but I don't think that there was a  
2 question in terms of the claims or at least the jurisdictional  
3 question, I guess, which is if there is no possible benefit to  
4 the estate then should this be something -- should this Court  
5 be enjoining -- should be requiring this particular result from  
6 Axis when either way there isn't going to be any possibility of  
7 a benefit to the estate even in the form of a reduced claim.  
8 That's the question, I guess.

9 THE COURT: Well, but it, I guess -- okay. Now I  
10 understand your point now. It's a jurisdictional point you're  
11 raising as opposed to a lifting of an injunction point.

12 MR. WILOMOWSKY: I think so, Your Honor.

13 THE COURT: But as far as jurisdiction goes, in  
14 addition to the narrow "benefit" issue, isn't there  
15 jurisdiction premised on the fact that the policy itself is  
16 property of the estate and I'm being asked to interpret it,  
17 and, secondly, the fact that it's one in a layering of excess  
18 coverage and at some point if the policy is interpreted  
19 properly and the facts play out properly in that layering -- in  
20 that sequence of layers the estate will benefit because there  
21 will be insurance that will pay claims either of D's and O's or  
22 of other claimants -- third parties -- who were, under the  
23 Plan, made the appropriate election to look to the litigation  
24 and, obviously, the insurance that is behind the litigation.

25 MR. WILOMOWSKY: I think that's right, Your Honor.

1 I think though that ironically though the granting of this  
2 motion is more likely -- if you assume -- if we don't present -  
3 -

4 THE COURT: No, but you see that goes to the  
5 merits as opposed to jurisdiction. I understand, but sometimes  
6 you have --

7 MR. WILOMOWSKY: I understand, Your Honor. That  
8 was it. I think I've said enough.

9 THE COURT: Okay.

10 MR. JEROME: Your Honor, may I be heard?

11 THE COURT: Yes.

12 MR. JEROME: Your Honor, I represent Joseph P.  
13 Murphy along with Baker, Hostetler. Mr. Murphy was an officer  
14 of Refco in charge of marketing and ran the regulated company,  
15 which as Your Honor may recall was sold in these bankruptcy  
16 proceedings. Now, Mr. Murphy, as an officer of Refco is  
17 unfortunately embroiled in the various class actions. He was  
18 also a beneficiary of the various insurance policies which are  
19 contested.

20 I think the dark and somewhat unstated fact here  
21 is that as the assets -- and I'm not saying that it shouldn't  
22 be done and that's not appropriate -- but equitably and fairly,  
23 the unhappy fact is that as assets are burned for criminal  
24 defense I have no doubt that the consequence of that will be  
25 that Mr. Murphy will not in fact have enough funds from

1 insurance proceeds to answer to any judgment that might be  
2 levied against him, and I also think he probably will not have  
3 sufficient funds to defend himself in the class actions given  
4 what I know and maybe my knowledge is deficient and Your Honor  
5 knows, sometimes that happens with me, but it may be I'm right  
6 and I think that I am.

7               So in terms of weighing the harm and the equities  
8 here, while I'm not suggesting that the criminal defendants are  
9 entitled to the relief that they seek here, I would like to  
10 suggest that there is an opportunity that we have, an  
11 opportunity of constricted time which we have between now and  
12 October 12th when Your Honor will be called upon to make a  
13 decision in respect of the permanent injunction. I would hope  
14 that in that constrained time frame we would, perhaps, resort  
15 to some form of mediation. And I know, Your Honor, the other  
16 insurance companies are not before you and I'm certainly not  
17 asking that this Court, although it has the power, to compel  
18 mediation. I'm suggesting that the parties in the interests of  
19 trying to iron out these various issues which will continue,  
20 Your Honor, to come before this Court, because each and every  
21 insurance company is going to deny coverage and is going to be  
22 before this Court or some other court arguing this for months  
23 on end, I think that if Your Honor would at least on the  
24 record, while not compelling arbitration, suggest that it might  
25 be a good idea for the parties to engage in between now and

1 October 12th and in addition to the parties, those other  
2 insurers who are not before Your Honor may at least get a  
3 friendly message which would encourage them to sit down and try  
4 to at least get the process started. I think that the result  
5 of an appropriately negotiated, successful mediation could  
6 result in evening out, I think, some of the tawdry races that  
7 we're witnessing in terms of first come/first serve, have you  
8 gotten your bills in or haven't you, and in point of fact,  
9 Mr. Murphy's \$13,000.00 bill for July wasn't filed on time. We  
10 were seven days late.

11 I know we'd like to avoid this and I think  
12 mediation, hopefully, if it could resolve these matters could  
13 resolve this, I think, unseemly race to the insurance  
14 courthouse. So, Your Honor, I would respectfully request that  
15 this Court at least on the record encourage the parties to come  
16 to some form of mediation. I might add that there has been  
17 some discussion between the parties on the subject and I think  
18 that some of them might be favorably disposed to doing so. If  
19 some of the parties fall out and don't want to do it, that  
20 doesn't mean that other parties involved, particularly my  
21 client, my shared client, couldn't benefit from the mediation,  
22 and in no way, shape or form, Your Honor, am I suggesting that  
23 the mediation would prejudice these proceedings or interfere  
24 with what's going to happen on October 12th. I am suggesting  
25 that we have a window of time, and I would hope that the Court

1 would encourage us and urge us to resort to mediation.

2 With that, Your Honor, I thank you very much for  
3 your indulgence.

4 THE COURT: Okay.

5 MR. EISEN: Your Honor, I have a couple of very  
6 brief points and then Ms. Moses will conclude on behalf of the  
7 insureds.

8 With respect to counsel for Mr. Murphy's  
9 statement, we wholeheartedly agree. I don't know that it is  
10 necessary or appropriate to be part of an order. I take it  
11 there's no disagreement as with the Debtor's position, they  
12 haven't objected to the relief we seek and we think that the  
13 idea of all sitting down and talking, bringing the other  
14 insurers to the table is a good idea. So, certainly, the  
15 movants today do not need to be ordered to do that. I do think  
16 that the counsel's statement does emphasize the value of  
17 issuing an order as of today that will apply to the payments of  
18 these fees so that this race is not to the disadvantage of  
19 some. Obviously, we think the disadvantage is greater as to  
20 the criminal defendants.

21 On the jurisdictional point that the Debtor  
22 raised, the Court responded more eloquently and knowledgeably  
23 than I can and I would only echo those points by saying, you  
24 know, it really is one dispute that all of the movants are  
25 queuing up for the Court. The Court has already found that it

1 has jurisdiction, and as the Debtor noted, Mr. Grant had filed  
2 the claims, they were disputed.

3 Then, finally, I looked back at whether it was  
4 agreed or not as to the means of the previous movants and in  
5 fact it was hotly contested. Axis made the point very  
6 forcefully that the previous insureds had not made a showing  
7 either that they can't pay or that they can repay, and the  
8 previous insureds replied with equal force that that is not the  
9 test and I think the Court will find that the record is  
10 completely devoid of that evidence because under WorldCom and  
11 under Your Honor's holding that showing is not required in a  
12 mega case of this kind and with that I will yield to my  
13 colleague.

14 MS. MOSES: Very briefly, Your Honor, and we do  
15 appreciate the time you've devoted to this matter this morning.

16 Mr. Jerome used the term "unseemly" with respect  
17 to the various insureds' request for defense payments. I think  
18 the only thing that can be said about that is that my client,  
19 Mr. Trosten, and the other indicted plaintiffs, Mr. Bennett and  
20 Mr. Grant, did not indict themselves. They did not choose to  
21 be criminal defendants, they are not --

22 THE COURT: Well, I think he was just talking  
23 about a rush to get bills in. I think that's all he meant by  
24 that.

25 MS. MOSES: Right.

1 MR. JEROME: That's correct, Your Honor. Thank  
2 you.

3 MS. MOSES: With respect to the mediation point,  
4 no lawyer wants to be in the position of resisting a suggestion  
5 of mediation and I certainly am not going to put myself in that  
6 position but I do think it is fair to point out that while  
7 the parties can and I hope they will voluntarily discuss a  
8 potential non-litigation solution to this issue between now and  
9 October 12th, nothing that we do between now and October 12th  
10 can stop the clock with respect to the underlying actions,  
11 either civil or criminal, and particularly given Axis' history  
12 of resisting to the very last moment and sometimes beyond and  
13 its demonstrated reluctance to write a check until and unless  
14 it is specifically ordered to do so by this Court, my own view,  
15 Your Honor, is that settlement discussions with an eye towards  
16 possibly a global settlement involving the higher tier carriers  
17 as well will be far more effective and far more likely to  
18 succeed after October 12th if, indeed, that is the date for  
19 summary judgment. Thank you.

20 THE COURT: Okay. Do you have anything to say,  
21 Ms. Gilbride?

22 MS. GILBRIDE: Yes, just very, very briefly, Your  
23 Honor.

24 With respect to the arguments advanced by both  
25 counsel that the WorldCom decision controls somehow, whether or



1 not Your Honor has to consider balancing of harms, I would just  
2 simply submit that the WorldCom court did not consider  
3 balancing of harms in any way, shape or form. It didn't say  
4 that you don't consider it, it simply wasn't considered. There  
5 is Second Circuit authority precisely on point which says that  
6 the balancing of harms must be considered when the Court orders  
7 a preliminary injunction.

8               With respect to the Catch-22 that counsel and Your  
9 Honor are concerned about, respectfully, there is a provision  
10 in the Federal Rules that deal with that precise issue, it's  
11 Rule 65(c), which states that when ordering a preliminary  
12 injunction a court can and should but has discretion, of  
13 course, order that the party who is being awarded the  
14 preliminary injunction either post a bond or securitize the  
15 amounts being awarded, and, respectfully, I think that that  
16 deals with the Catch-22 situation that counsel is referring to  
17 and, perhaps, was meant for just that situation.

18               With respect to the priority of payments issue,  
19 Your Honor, I haven't had a chance to confer with Baker &  
20 Hostetler but if Your Honor so desires a copy of the MOU in  
21 camera with consent of counsel, we'd be happy to submit that to  
22 you if you so desire.

23               I have nothing further. Thank you.

24               THE COURT: Okay.

25               MR. EISEN: Your Honor, could I just respond to

1 the WorldCom point, because it is in the case.

2 THE COURT: No, I read -- I know.

3 I'm going to take a look at Judge Woods' decision,  
4 so you can hand that up to me and I'm going to take a break,  
5 but before I do that I'm going to deal with the two pre-trials  
6 that I put at the end of the calendar and then I'll come back  
7 to you all probably by -- hopefully, by 12:00 or 12:15, so you  
8 can check your Blackberrys and make some phone calls and I'll  
9 be back around 12:15 or so, is my guess, with a ruling.

10 ALL ATTORNEYS: Thank you, Your Honor.

11 THE COURT: So if you could hand that up and then  
12 I'll take the American Express v. Rodriguez or Gloria Ramirez.

13 [Off the record.]

14 THE CLERK: Please be seated.

15 THE COURT: Before the Court is a motion for a  
16 preliminary injunction brought by Messrs. Grant, Trosten and  
17 Bennett in this adversary proceeding in which they are  
18 ultimately seeking a declaratory judgment and permanent  
19 injunction against Axis Reinsurance Company, an excess insurer  
20 that is currently in line in the tiers of insurance coverage  
21 obtained by the debtor, Refco, Inc., for its officers and  
22 directors and itself.

23 Procedurally, I should go through the history of  
24 this matter briefly. The first step in respect of this  
25 insurance company or insurance coverage dispute was taken by

1 Axis in initiating an adversary proceeding against not only  
2 Grant, Trosten and Bennett but the other officers and directors  
3 of Refco, Inc. who have made claims in respect of the policy,  
4 as well as Refco, for a declaratory judgment that Axis was not  
5 obligated to pay under the policy.

6 That was followed by different responses by  
7 various groups of defendants. First, one group of defendants  
8 represented by Weil, Gotshal moved to dismiss Axis' adversary  
9 complaint. Second, another group of officers and directors made  
10 a counterclaim for the advancement of defense costs, and third,  
11 the present group, Grant, Trosten and Bennett, joined in or  
12 purported to join in both of those requests for relief. I  
13 granted the motion to dismiss Axis' request for a declaratory  
14 judgment as to its obligations generally under the policy to  
15 provide coverage on the basis of the so-called "substantial  
16 overlap" doctrine as set forth in numerous cases, including by  
17 Judge Cote in In re: WorldCom, Inc. Securities Litigation, 2002  
18 W.L. 31729501 (S.D.N.Y., December 5, 2002), as well as in  
19 Adelphia and Enron.

20 The basis set forth in my bench ruling was that  
21 ultimately the facts that Axis would need to establish to  
22 prevail on its claim and, to the contrary, the facts that the  
23 defendants would need to refute to defeat Axis' claim  
24 substantially overlap with facts that would also in all  
25 likelihood arise in the pending securities litigation before

1 District Judge Lynch, as well as, potentially, in the District  
2 Court criminal litigation against Grant, Trosten and Bennett.

3 Turning then to the counterclaim and related  
4 request for a preliminary injunction, I determined that there  
5 was a likelihood of success on the merits and irreparable harm  
6 and, absent such, sufficient questions going to the merits and  
7 the balance of harms in favor of the counter-claimants to  
8 support an injunction requiring the advancement of their  
9 defense costs billed through the date of my order.

10 However, I also concluded that procedurally the  
11 request for the same relief by Messrs. Grant, Trosten and  
12 Bennett was not properly before me, as they themselves had not  
13 made a counterclaim and there was no adversary proceeding  
14 asserting their claims against Axis and, consequently, no basis  
15 for granting them a preliminary injunction. They subsequently  
16 remedied that procedural defect by commencing an adversary  
17 proceeding and seeking and obtaining an expedited hearing on  
18 their motion for a preliminary injunction for the advancement  
19 of defense costs.

20 I should note as an aside that the parties should,  
21 unless I'm missing something, promptly consolidate this  
22 adversary proceeding with the counterclaim, which is now its  
23 own adversary proceeding brought by the defendants represented  
24 in part by Baker & Hostetler.

25 I won't go over at length the findings that I made

1 and the rulings that I made at the prior hearing. They're set  
2 forth in the transcript -- which I've reviewed as far as typos  
3 and misheard words are concerned and corrected, and I hope  
4 that's what the parties have. I think it is.

5 I'll note that there was a procedural matter that  
6 -- consistent with some of my remarks on the record, Axis has  
7 subsequently moved in the District Court for withdrawal of the  
8 reference of the adversary proceeding, and that well may be  
9 heard before the hearing that I've scheduled for mid-October on  
10 the ultimate relief requested by the counterclaim plaintiffs  
11 and by Grant, Trosten and Bennett against Axis.

12 However, pending a determination of that motion  
13 for withdrawal of the reference, I continue to have  
14 jurisdiction and, as noted at the prior hearing and I think as  
15 reiterated today in the colloquy with counsel for the Refco  
16 plan administrators, I believe I have jurisdiction over this  
17 matter and this adversary proceeding because it is one in which  
18 I am asked to interpret the provisions of the Axis policy,  
19 which is property of the debtor's estate, and, secondly,  
20 because the payments under the policy affect distributions to  
21 creditors of this estate, either creditors with indemnification  
22 claims such as the directors and officers or, perhaps,  
23 ultimately, securities law creditors and others who have made  
24 claims not only against Refco but also against officers and  
25 directors and under the plan agreed to a mechanism for pursuing

1 those claims jointly with the Refco estate.

2 This motion before me also seeks relief from --  
3 what it says is the automatic stay -- to permit payment of the  
4 insurance proceeds in respect of the advancement of defense  
5 costs, which is also a "core" matter. However, as I noted at  
6 the last hearing, Paragraph 34 of the confirmation order  
7 provides that the automatic stay itself is no longer in place.  
8 However, it also notes that it does not otherwise amend the  
9 Plan and the other provisions of the confirmation order, which  
10 does contain its own plan injunction which may be implicated by  
11 the payment of the defense costs.

12 In any event, because of that request, which I am  
13 taking as a request for relief from the Plan injunction as  
14 opposed to from the automatic stay, I also, as a third basis,  
15 have jurisdiction here because ultimately I'm being asked to  
16 interpret the Plan and enforce the Plan by considering relief  
17 from the injunction in the Plan.

18 In short, the basis for the request for a  
19 preliminary injunction is the movants' contention that under  
20 the applicable insurance policies, which include the primary  
21 policies as incorporated in the Axis policy, Axis is obligated  
22 to advance, that is pay, defense costs, subject to  
23 reimbursement if it's ultimately concluded that such defense  
24 costs were not covered under the policy.

25 The movants contend that that contractual language

1 when coupled with the various presumptions regarding  
2 interpretation of insurance policies under New York law  
3 particularly provisions of insurance policies dealing with  
4 exclusions and dealing with defense costs -- is clear and that  
5 there's a substantial likelihood that they would prevail on the  
6 merits.

7           They also contend that given the amount of defense  
8 costs that have been incurred to date and the fact that they  
9 are criminal defendants subject to freeze orders, the failure  
10 to advance the defense costs irreparably harms them in that it  
11 impairs their ability to mount an effective defense, in this  
12 case of a criminal indictment.

13           They also contend that even if they were not a  
14 substantial likelihood of success the balance of harms tips in  
15 their favor given the foregoing contentions and the opposite  
16 consideration that Axis is a very substantial corporation and  
17 that it agreed to make these payments and take the risk of non-  
18 payment in the policy.

19           Finally, they state, as a matter of public policy,  
20 they should not be saddled with the payment of the defense  
21 costs since that would vitiate the purpose of a D&O policy and  
22 ultimately discourage parties from serving as officers and  
23 directors of a corporation.

24           They have not presented any other evidence than  
25 the amount of the defense costs and the fact that they are

1 facing a criminal trial in March of 2008 and the request for me  
2 to take judicial notice of freeze orders. That is, they've not  
3 offered evidence as to their financial condition or their law  
4 firms' willingness to work with the overhanging uncertainty as  
5 to whether they would ultimately be paid for conducting the  
6 movants' defense.

7 Axis has responded by, first, disputing that there  
8 is a substantial likelihood that the movants would ultimately  
9 prevail on the merits. It is also contended that as a factual  
10 matter irreparable harm has not been shown and that neither has  
11 a balance of the equities tipping in favor of or a balance of  
12 the harms tipping in favor of the movants. They also contend  
13 that the public policy cited by some of the courts that have  
14 previously considered this issue is less significant where an  
15 officer and director is the subject of a criminal indictment  
16 and is being defended in a criminal proceeding. It has sought  
17 a bond under Rule 65(c), as well.

18 Finally, it has contended that the relief that is  
19 sought here is fundamentally inequitable because the movants  
20 had previously joined in the motion, which was successful, to  
21 dismiss Axis' declaratory judgment complaint.

22 As far as the amount of the defense costs is  
23 concerned, I believe the record is now clear that through the  
24 date of my prior injunction order, August 31st, the cost billed  
25 was approximately \$1.6 million for these three movants and that



1 it is approximately \$2.9 million as of today. The policy  
2 itself has a \$10 million limit.

3           Clearly, as far as these defendants are concerned,  
4 they have been in serious litigation mode with very large  
5 defense costs being incurred since July of this year, and it is  
6 likely that that will continue over the next several months as  
7 they prepare for trial in what appears to be a complex, at  
8 least as a factual matter, case. And I'll note in that regard  
9 that I take judicial notice of the cost incurred by the Refco  
10 estate of examining the facts and circumstances surrounding the  
11 claims that at least overlap with the claims against  
12 Mr. Bennett and the other two criminal defendants, costs which  
13 I had to approve before they were paid.

14           Let me turn to the last point raised by Axis  
15 first. I concluded last week that it is not inequitable to  
16 proceed with this type of claim and to grant preliminary  
17 injunctive relief notwithstanding the movants' prior request to  
18 dismiss Axis' complaint, although they along with Weil, Gotshal  
19 were successful in that request or the Weil, Gotshal defendants  
20 were successful in that request. I do not believe there is a  
21 basis for judicial estoppel here because I believe that the  
22 issues pertaining to the motion to dismiss are fundamentally  
23 different than the issues presented by the claim asserted in  
24 the present adversary proceeding as well as the counterclaim  
25 asserted by the other defendants.

1           As I noted previously, the basis for this request  
2   is one in which I need not consider the factual issues that  
3   overlap with the District Court securities litigation and the  
4   criminal litigation but rather need only consider the language  
5   of the contract, that is the insurance policies and the related  
6   warranty, and applicable case law. If, in fact, I were to  
7   conclude ultimately that Axis was not obligated to advance  
8   defense costs but could withhold those costs pending a  
9   determination as to whether they were -- whether Axis would be  
10   successful in concluding that this denial of coverage was  
11   appropriate and correct, then there would be an overlap and at  
12   that point this adversary proceeding and the adversary  
13   proceeding brought by the counterclaim parties would be either  
14   stayed or dismissed without prejudice pending the development  
15   of those facts in the multi-district securities litigation  
16   and/or the criminal case. But I believe I can -- and unless  
17   the reference is withdrawn, I must -- consider whether as a  
18   matter of reading the insurance policies and the case law and  
19   the related warranty whether there is a separate obligation to  
20   advance defense costs prior to determination of the underlying  
21   coverage dispute based on whether there was a misrepresent -- a  
22   breach of the representation -- a breach of the so-called  
23   warranty and/or the exclusions in the policy relied upon by  
24   Axis for disclaimer of coverage apply.

25           Turning then to the other defenses raised by Axis,

1 let me address first the appropriate standard by which I should  
2 consider the motion here for a preliminary injunction. Axis  
3 contends that because the relief sought here is one in which  
4 Axis would be compelled to advance defense costs, this is a  
5 request for mandatory injunctive relief rather than for a  
6 prohibitory injunction. Consequently, Axis argues, I need to  
7 consider the request pursuant to a heightened standard that  
8 applies to mandatory injunctions -- where I would have to find  
9 on the merits a substantial likelihood that the plaintiffs  
10 would ultimately prevail. See, for example, Tom Doherty  
11 Associates, Inc. v. Saban Entertainment, Inc., 60 F.3d 27, 35  
12 (2d Cir. 1995). In that case, the Second Circuit noted that  
13 the distinction between a mandatory and a prohibitory  
14 injunction has been the subject of criticism and particularly  
15 noted the criticism of that standard in respect of breach of  
16 contract cases where one party's assertion that the status quo  
17 is merely being maintained is another party's assertion that  
18 that party is actually breaching the status quo by breaching  
19 the underlying agreement.

20 This very issue was addressed by what I believe to  
21 be the leading case, or the most relevant case to the issues  
22 before me, that is Judge Cote's opinion in In re: WorldCom,  
23 Inc. Securities Litigation, 354 F. Supp. 2d. 455 (S.D.N.Y.  
24 2005) in which she concluded ultimately that the heightened  
25 standard for a preliminary mandatory injunction does not apply

1 to a motion for a preliminary injunction for the advancement of  
2 defense costs, for the reason that -- for the reasons that she  
3 lays out at Page 463 of that opinion. She notes first that in  
4 that matter, as well as here, given that the amount at issue is  
5 well under the policy limit that a preliminary injunction would  
6 not make it difficult or impossible to render a meaningful  
7 remedy to a defendant who prevails on the merits at trial, and  
8 that only part of the benefits to which the directors, in this  
9 case the directors and officers, are seeking ultimately would  
10 be covered here in the injunction. And, secondly, that the  
11 policy itself contemplated reimbursement.

12 That view was also recently followed in Great  
13 American Insurance Company v. Gross, 2005 U.S. District Lexis  
14 8003 (E.D. Va., May 3, 2005), which was vacated on other  
15 grounds, 468 F. 3d 199 (4th Cir. 2006).

16 So I don't believe that I must follow the  
17 heightened standard requiring the finding of clear likelihood  
18 or a substantial likelihood of success on the merits.  
19 Nevertheless, I have considered obviously whether there would  
20 be a likelihood of success on the merits, as did Judge Cote in  
21 the WorldCom case, but did not limit my inquiry to that  
22 analysis but considered also the regular standard.

23 I conclude that, as did Judge Cote, in her words,  
24 nevertheless even if the heightened standard applies I believe  
25 that the movants here have established a clear likelihood of

1 success on the merits.

2 Let me turn to the merits now. As Judge Cote  
3 recognized, under New York law (and as an aside I previously  
4 concluded that New York law should apply to disputes in respect  
5 of this insurance coverage for the reasons set forth in my  
6 earlier bench ruling), while the plain language of an insurance  
7 agreement, as with any contract covered by New York law, is the  
8 best evidence, and, if unambiguous, the only evidence, of the  
9 parties' intentions, as a matter of law for the Court to  
10 decide, in respect of insurance contracts, to the extent an  
11 ambiguity exists and is unresolved by extrinsic evidence, such  
12 ambiguity is read against the insurer. The rule that insurance  
13 policies are to be construed in favor of the insured is most  
14 rigorously applied in construing the meaning of exclusions  
15 incorporated into a policy of insurance or provisions seeking  
16 to narrow the insurer's liability. And, finally, that where a  
17 contract of insurance includes the duty to defend or to pay for  
18 the defense of its insured that duty is a "heavy" one.

19 As set forth by Judge Cote, in addition under New  
20 York law, including as interpreted by the Appellate Division in  
21 the Kozlowski/Tyco case, as well as by numerous Southern  
22 District courts, the duty of an insurer to pay an insured's  
23 defense costs is distinct from and broader than its duty  
24 ultimately to indemnify. Even where the policy does not provide  
25 specifically for when defense costs are to be advanced, it has

1 been held that they need to be advanced as incurred under a  
2 liability policy as set forth in Judge Baer's Nu-Way decision.

3 Moreover, it appears clear to me under New York  
4 law that the duty to pay defense costs exists whenever a  
5 complaint against the insured alleges claims that may be  
6 covered under the insurer's policy. That is, if it appears  
7 from the face of the underlying complaint against the insured  
8 that there is an issue as to whether that complaint sets forth  
9 a claim that may be covered the costs would need to be  
10 advanced. See, for example, the Kozlowski/Tyco case as well as  
11 the Nu-Way decision, which appears at 1997 U.S. District Lexis  
12 11884 (S.D.N.Y. August 12, 1997).

13 The opposition to the motion by Axis attempts to  
14 make a distinction between situations where the courts have  
15 considered a refusal to pay defense costs because the insurer  
16 has sought or has taken the position that the policy was  
17 rescinded. It has also taken the position that there should be  
18 a distinction between the present matter and decisions which  
19 have dealt with the duty to defend as opposed to a duty to  
20 advance defense costs. But I conclude based on my review of  
21 the case law that where an insurer takes the position that a  
22 claim is not covered and therefore it is not obligated to  
23 advance defense costs those distinctions are not meaningful, in  
24 that they apply in cases of rescission, cases where there's an  
25 alleged obligation to advance and cases where there's an

1 alleged obligation to defend.

2 For example, in the Tyco/Kozlowski matter the  
3 insurer alleged that the underlying claims were not covered and  
4 therefore the defense costs would not be covered either. The  
5 Court held, however, that unless the insurer has no duty as a  
6 matter of law it would have an obligation to advance the  
7 defense costs, stating that the duty to defend or pay defense  
8 costs is construed liberally and any doubts about coverage are  
9 resolved in the insured's favor. Furthermore, an insurer can  
10 only invoke a policy exclusion to avoid coverage if it can show  
11 that the allegations in the complaint casts that pleading  
12 solely and entirely within the policy exclusions. The duty to  
13 defend arises when the action is brought and is unaffected by  
14 the outcome of the action. See, also, Pepsico, Inc. v.  
15 Continental Casualty Company (S.D.N.Y. 1986), McGinnis v.  
16 Employer's Reinsurance Corporation, 648 F. Supp. 1263 (S.D.N.Y.  
17 1986); The Great American Insurance Company v. Gross case that  
18 I referred to earlier and G1 Holdings, Inc. v. Heyman -- I'm  
19 sorry, G1 Holdings, Inc. v. Reliance Insurance Company, 2006  
20 U.S. District Lexis 17597 (D. New Jersey, March 22, 2006).

21 Axis' response, in addition to saying that it need  
22 not advance the costs pending resolution of the dispute, is  
23 that it is clear from the language of the insurance policy  
24 itself that there is no way that it would be obligated to  
25 provide coverage here.

1           As I noted in my prior ruling on the earlier  
2 request for an injunction, this is ultimately premised upon  
3 Axis' reading of Paragraph D2 of the underlying policy which  
4 states that "the insurer will pay covered defense costs on an  
5 as incurred basis. If it is finally determined that any  
6 defense costs paid by the insurer are not covered under this  
7 policy the insured's agree to repay such non covered defense  
8 costs to the insurer." Axis contends that because of the word  
9 "covered" in the first sentence, it need not pay costs that are  
10 not covered under the policy.

11           I conclude that it is likely that that  
12 interpretation will not prevail, given the foregoing case law  
13 as well as the provision when read as a whole, which, first,  
14 requires the insurer to pay covered defense costs "on an as  
15 incurred basis," i.e. not waiting until an ultimate  
16 determination, but as incurred with out of pocket payment, and,  
17 secondly, the second sentence, which provides for reimbursement  
18 if it is finally determined that any defense costs paid by the  
19 insurer were not covered.

20           Axis contends that the word covered in the first sentence  
21 has to mean "covered" by the policy but I have two responses to  
22 that. The first is that I see little difference between that  
23 argument and an argument that says that, as in the cases that I  
24 previously cited, a defense cost falls into an exclusion  
25 because it's not for costs determined to have arisen from



1 defense of a claim covered by a policy -- i.e. the policy, it  
2 was argued in those other cases, doesn't cover certain types of  
3 claims and, therefore, the defense costs also would not fall  
4 into the coverage of the policy. Notwithstanding those  
5 arguments, courts like the Kozlowski court determined that the  
6 costs should be advanced pending ultimate determination of that  
7 issue.

8               Secondly, "covered" -- when one looks at the  
9 definition of defense costs and loss in the first sentence --  
10 "covered," as used in the first sentence after looking at those  
11 definitions, could mean whether it pertained to "insured  
12 persons," or not, or whether those persons had become "legally  
13 obligated," or not, to make the payments of their defense  
14 costs.

15               So, in any event, I believe that ultimately it is  
16 likely that the movants here would prevail on the merits. I  
17 conclude that the following paragraph of the policy, which  
18 deals with the allocation of losses covered and losses not  
19 covered by the policy, does little to advance Axis'  
20 interpretation and may slightly advance the movants' in that it  
21 would seem to be superfluous if Axis' interpretation were the  
22 correct one. That is, you would not need to provide for a  
23 distinction between losses covered and losses not covered if  
24 the insurer could withhold under Paragraph D2, defense costs  
25 that it believed were not covered.

1 I do not believe the language, which, again,  
2 requires payment on an "as incurred," basis is materially  
3 different from the language quoted by Judge Cote in the  
4 WorldCom case and would need to be far clearer to create an  
5 exclusion here.

6 Turning to the issue of irreparable harm, Judge  
7 Cote found in WorldCom that wherever individual officers and  
8 directors were faced with substantial defense costs that were  
9 not being paid, they would -- they were subject to irreparable  
10 harm. As she says, "it is impossible to quantify the impact on  
11 a litigant of a failure to have adequate representation at this  
12 critical stage of litigation. The ability to mount a  
13 successful defense requires competent and diligent  
14 representation. The impact of an adverse judgment will have  
15 ramifications beyond the money that will necessarily be  
16 involved." That's especially true, as noted by Judge Gerber in  
17 the Adelphia/Regis case where the insured or the beneficiary of  
18 the policy is the subject of a criminal proceeding.

19 Judge Cote is not alone in finding irreparable  
20 harm in these circumstances. It was also found in the G1 and  
21 Gross cases that I cited earlier, as well as in McPeck v.  
22 Travelers Casualty & Surety Company of America, 2006 U.S.  
23 District  
24 Lexis -- I'm sorry, excuse me. Let me back up.

25 It was recognized in the Bondex International,

1 Inc. v. Hartford Accident & Indemnity Company case, 2006 U.S.  
2 District Lexis 50083 (N.D. Ohio, July 21, 2006), to apply in a  
3 case of an individual beneficiary or insured under a director's  
4 and officer's policy but would not apply to a corporation, at  
5 least absent evidence of insolvency, which again I believe  
6 heightens or puts a fine point upon the burden faced by an  
7 individual here.

8           There is one case that takes a contrary view, and  
9 that is the McPeck case that I started to cite earlier. McPeck  
10 v. Travelers Casualty & Surety Company of America, 2006 U.S.  
11 District Lexis 28619 (W.D. Penn., May 10, 2006), in which the  
12 court found there was not irreparable harm because there had  
13 not been a showing, a factual showing, that the beneficiaries  
14 there would be unable to mount a defense.

15           There may conceivably be circumstances where an  
16 additional factual showing would need to be made to establish  
17 irreparable harm in this context, but I believe that there's a  
18 sufficient record before me to show irreparable harm given the  
19 substantial amount of the defense costs, the freezing of the  
20 defendants' assets and the fact that they're subject to  
21 criminal exposure. So to the extent that I find McPeck at all  
22 persuasive, I believe it's distinguished under the present  
23 circumstances.

24           As did Judge Cote, therefore, I've concluded, although I  
25 do not believe the heightened standard needs to apply, that the

1 movants meet it here.

2 Turning, however, to the ordinary standard for a  
3 preliminary injunction, I've already discussed the merits, and  
4 even if one were not to take the view that there was a clear or  
5 substantial likelihood of success, for the reasons I've stated  
6 I believe there is definitely sufficient a issue going to the  
7 merits that I would turn then to the balance of harms, as the  
8 merits are fair ground for litigation.

9 I conclude that the balance of harms tips  
10 decidedly in favor of the movants here. I believe that  
11 although she did not have a heading in her opinion in which she  
12 balanced the harms, Judge Cote did consider the harm not only  
13 to the movant in not granting injunctive relief but also the  
14 potential harm to the insurer were she to grant the relief, and  
15 concluded, as I conclude here, that the balance of harms tips  
16 decidedly in favor of the movant and that, as she discussed,  
17 the fact that the -- in her belief there was no undue hardship  
18 on the insurer as its liability is ultimately capped and,  
19 secondly, that the policy set out a mechanism that the insurer  
20 bargained for for reimbursement ultimately and that  
21 particularly in light of the potential harm to the movant and  
22 the public interest in favor of advancing the defense costs,  
23 the insurer should not be entitled to more.

24 In a more explicit analysis both the McPeck and  
25 Great American v. Gross cases similarly found a balance of

1 harms tipping in favor of the movant as well as the public  
2 interest being in favor of the movant.

3 As noted at oral argument, Axis had cited to me an  
4 unpublished -- including not appearing on either Lexis or  
5 Westlaw -- ruling by Judge Wood in a civil matter, Gaon v. Twin  
6 City Fire Insurance Company. I've reviewed that,  
7 notwithstanding the Second Circuit's rule on citation to  
8 unpublished opinions and the fact that a copy of the ruling was  
9 not obtainable by the Court or provided to the Court prior to  
10 oral argument, and I conclude, first, that the decision by  
11 Judge Wood is distinguishable in that she had, to my mind, a  
12 far different view of the underlying merits of the case, which  
13 was a very different case than the case before me. I note  
14 further that while she mused that cases such as WorldCom may  
15 not have considered sufficiently the balance of harms or the  
16 balance of the equities, I do not view her as ultimately ruling  
17 on that basis.

18 In any event, again, as I distinguished the McPeck  
19 case, I believe that the amount at issue here and the fact that  
20 this is a criminal matter distinguish the present matter from  
21 Gaon.

22 As far as Axis' request that the movants post a  
23 bond under Rule 65(c) incorporated by Rule 7065, I again follow  
24 the logic set forth by Judge Cote in WorldCom, which was also  
25 adopted by the Great American v. Gross and G1 cases that I

1 cited earlier: effectively, to require a bond here in my view  
2 would vitiate the entire ruling, particularly since these are  
3 individual defendants. In essence, it would under the guise of  
4 obtaining a bond require the movants to pay for insurance all  
5 over again, notwithstanding the language of the policy.

6 So I exercise my discretion not to require a bond  
7 in these circumstances. I do so also mindful that the amount  
8 that I'm going to require to be advanced is well within the  
9 capped amount of the policy and that, as I noted earlier, the  
10 ultimate issues here are teed up for a final determination in  
11 31 days, and that leads into the last part of my ruling.

12 It was requested by Axis that I rule as to the  
13 proper allocation or priority of payment of funds directed to  
14 be paid, if any, by me. I do not believe that request is  
15 appropriately before me, given the seriousness of it, the  
16 parties who would be affected by it, and the limited amount of  
17 notice. As importantly, I don't believe it's a ripe question,  
18 because I don't believe any other priority or any priority  
19 issues are necessarily determined by my ruling today, and,  
20 further, although this is not critical to my ruling, I don't  
21 believe that my ruling today would put Axis in a position of  
22 acting at its peril and paying out one way or another under the  
23 policy, which it has generally disclaimed and refused to pay  
24 out under, absent a judicial ruling requiring it to do so.

25 It appears to me that, therefore, an order

1 requiring payment with a full reservation of rights as to the  
2 allocation, or priority, of payment generally under the policy  
3 is appropriate. I've determined, given the record as to the  
4 billing of costs and the incurrence of costs, that it would be  
5 appropriate to require Axis to advance the defense costs to  
6 these three movants billed through the date of my prior order  
7 so that there's no, if you will, acceleration of billing, and  
8 that in my view the costs through the date of the prior order  
9 were in large measure billed in the ordinary course and I think  
10 appropriately paid.

11 I also believe that requiring the payment through  
12 that date puts these three movants on an even footing with the  
13 other movants who previously obtained the preliminary  
14 injunction. Given that I will be ruling, unless the reference  
15 is withdrawn, at or around October 12th, I believe that my  
16 present ruling would provide sufficient comfort to the law  
17 firms defending these three individuals that they will continue  
18 to provide the same level of service going forward without the  
19 necessity of paying them the additional amounts that have been  
20 billed starting in September and through today and that such  
21 payments would not be necessary to avoid irreparable harm in  
22 light of this ruling.

23 So it has been represented by counsel for the  
24 movants that they would propose an order that's substantially  
25 similar if not precisely similar to the prior injunction that I

1 had entered. I believe it would contain the language about,  
2 though, the reservation and preservation of all issues as to  
3 priority of payment. Have you -- do you have such an order?

4 MR. EISEN: Your Honor, I have the following order.  
5 I also have a disk. This order is identical other than  
6 changing the identities of the parties. I provided a copy to  
7 Ms. Gilbride and I provided a copy to Ms. Kim before the  
8 hearing today. If the Court likes as last time I can hand this  
9 draft up and the Court can --

10 THE COURT: Does it have the language about the  
11 reservation of rights as to priority?

12 MR. EISEN: It does not have the language about  
13 reservations of rights.

14 THE COURT: All right. Well, you should consider  
15 the injunction effective as of today but I think you should  
16 circulate that language because I think it's meaningful to the  
17 parties and you can submit an order tomorrow. It's 1:20 now.  
18 You may get it in today, but submit it with that language. You  
19 don't have to settle it on the parties but they'll have some  
20 time. You should email it to them at the same time you submit  
21 it to Chambers. They can tell me if it doesn't agree with my  
22 ruling.

23 MR. EISEN: I will, Your Honor.

24 MS. GILBRIDE: Your Honor, given the amount of  
25 money involved and the fact that we've only recently received



1 most of these bills, Axis would respectfully request a  
2 reasonable amount of time to review the bills and --

3 THE COURT: It's the same as the last ruling. I  
4 think it's -- it doesn't change anything as far as the policy,  
5 as far as your other rights under the policy including  
6 reviewing the bills, et cetera.

7 MS. GILBRIDE: It's just the turnaround time.  
8 Since we've just gotten the bills it does take a little bit of  
9 time to review the bills.

10 THE COURT: Again, this doesn't change that. I'm  
11 not saying you pay them tomorrow.

12 MS. GILBRIDE: I think the order says that we pay  
13 them within ten days of the order.

14 MR. EISEN: Your Honor, if I understand the Court  
15 correctly, it's only the bills that were presented to Axis as  
16 of the Court's previous --

17 THE COURT: The date was August 31st.

18 MR. EISEN: August 31st.

19 MS. GILBRIDE: Presented to us or through that day?

20 THE COURT: Yes, billed. Billed.

21 MR. EISEN: It's that the -- what I understood the  
22 Court to be saying was the insurers had -- if the insurer had  
23 the bills in hand as of August 31.

24 THE COURT: Okay.

25 MS. GILBRIDE: Thank you.

1 THE COURT: Now, as far as -- I know we're having -  
2 - I had previously scheduled a telephonic conference on the  
3 14th. I saw the result in front of Judge Koetl. I don't know  
4 whether there will be a motion for a stay or not. I don't know  
5 where you're going with withdrawal of the reference but I would  
6 like to keep this on track for the 12th. So --

7 MS. KIM: Yes, Your Honor, that is our intention  
8 to keep the motion for summary --

9 THE COURT: So I think we should still have that  
10 conference on the 14th.

11 MS. KIM: That's fine, Your Honor. With respect to  
12 Judge Koeltl, Judge -- we had an oral argument last Wednesday.

13 THE COURT: I read the -- someone attached the  
14 transcript and the ruling. So I'm up to date on that I think  
15 unless there -- I read what was attached to the exhibit as an  
16 exhibit.

17 MS. KIM: Well, actually that transcript, Axis  
18 submitted a letter --

19 THE COURT: I saw that. I saw that. Very well.  
20 Mr. Jerome raised the issue of mediation. This is perhaps an  
21 appropriate thing for the parties to do it. I did not hear  
22 Axis say whether it would be amenable to mediation or not. I  
23 think it would need to include the other insurers. It seems to  
24 me that the parties should consider mediation, but I don't  
25 believe that these issues should be put on hold unless there is

1 substantial progress in such a mediation. It seems to me that,  
2 as I noted at the last hearing --

3 MS. GILBRIDE: Just so Your Honor is clear, it was  
4 actually Axis' suggestion initially.

5 THE COURT: That's fine. I'm happy if Axis wants  
6 to mediate, but I think there are other insurers involved and  
7 that would be fine to have happen but there's a -- I believe  
8 there's a legal regime that governs in this area where insurers  
9 refuse to pay under policies and the parties are free to  
10 mediate but that legal regime governs and I think it needs to  
11 be followed because there are consequences beyond just a ruling  
12 by the Court as to whether the insured failed to pay or not.  
13 So I'm not going to hold off in the litigation unless there's  
14 substantial progress on a mediation, and I encourage the  
15 parties to try to make substantial progress on it. But I'm  
16 afraid "the parties" means not just Axis but other parties.  
17 This is not a litigation matter. This is a mediation matter  
18 and I think, as a practical matter, to mediate it you're going  
19 to need other parties, the other insurers.

20 Ms. Kim.

21 MS. KIM: Your Honor, just one last housekeeping  
22 matter. Our intervention motion, I don't think anyone -- no  
23 one opposed it. So if you could just --

24 THE COURT: That's fine. I obviously heard you  
25 all. Again, the two proceedings should be consolidated, I

1 believe. They raise the same issues in terms of interpreting  
2 the contract at least.

3 MR. EISEN: Your Honor, we would move for  
4 consolidation. If the Court wants to order that now then we'll  
5 take the appropriate steps with the clerk.

6 THE COURT: Do you want to think about that?

7 MS. GILBRIDE: Your Honor, we would appreciate an  
8 opportunity to consider that.

9 THE COURT: That's fine. That's fine. It seems to  
10 me it's sort of --

11 MR. EISEN: Thank you, Your Honor.

12 \* \* \* \* \*

13

14

15

16

17

18

19

20

21

22

23

24

25

1 I certify that the foregoing is a court transcript from  
2 an electronic sound recording of the proceedings in the above-  
3 entitled matter, except where, as indicated, the Court has  
4 modified the transcript.

5  
6  
7 

---

Shari Riemer

8 Dated: September 12, 2007  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25